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THE NEW ONTARIO HYDRO:

Year End Progress Report





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MESSAGE FROM THE CHAIRMAN

The past year was a very difficult one for Ontario Hydro. However, the overall restructuring of the Corporation into more business-like operating units has begun to pay off this year and will position us to meet our commitments in the coming years.

In March, 1993 the Corporation made a number of specific pledges. In the fall we issued a Progress Report which outlined the status of those pledges. Now we want to share with you the substantial progress Ontario Hydro has made since last fall, and also introduce further cost-saving strategies which are being implemented.

In all areas, Ontario Hydro is continuing with the initiatives to place itself on a sounder financial footing. In December 1993 Ontario Hydro's Board of Directors approved the consolidation of its three equity accounts into a single retained earnings account. In January 1994, the board approved a total restructuring provision in the range of \$2.9 to \$3.5 billion to be charged to net income which will be applied against the retained earnings account. By charging this one-time restructuring provision now, Hydro will avoid deferring these costs for

recovery out of rates over future years. This accounting method is consistent with that taken by commercial enterprises as a result of major restructuring initiatives.

After taking these provisions into account, the company begins 1994 with retained earnings in excess of \$4 billion. The Corporation's restructuring program is being viewed favourably by the financial community, with the Moody's and Standard and Poor's credit rating agencies maintaining their rating on Ontario Hydro's debt.

As we stated in our last Progress Report, there will be no rate increase in 1994, and we are confident that our goal of zero real rate increases for the rest of the decade will be achieved.

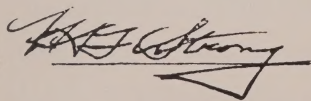
The coming year will be a period of consolidation and continuing change as we strive to ensure that Ontario Hydro is positioned to meet the needs of its customers in a new era of competitiveness and efficiency.

To that end, Hydro sponsored an International Symposium on the Future of the Electrical Power Industry in

Toronto February 7 and 8. This symposium was a working meeting targeted at developing and discussing short and long term alternatives to traditional utility structures. It brought together expertise from many sectors with the aim of contributing to the dialogue on the future of the electric power industry in Ontario.

Ontario Hydro is also progressing with its plans to expand its international activities through Ontario Hydro International and to develop more commercial opportunities from its extensive research and development capabilities through Ontario Hydro Technologies. In both of these it is striving to further its leadership role in energy efficiency and sustainable development.

There is still much to be done. However I believe the Corporation is on the right track and that the new Ontario Hydro will emerge as a world leader in the energy business. We will continue to monitor our progress closely and provide timely and candid reports.

A handwritten signature in dark ink, appearing to read "Maurice F. Strong", with a stylized flourish underneath.

Maurice F. Strong
Chairman and CEO

P L E D G E S

These are the pledges made by Ontario Hydro in 1993. The following pages provide news on the Corporation's progress in achieving these pledges and additional progress made in other areas.

- *There will be no rate increase in 1994 and a freeze in rates in real terms for the remainder of the decade.*
- *The Corporation will be restructured to make it more cost effective, accountable, and market-oriented.*
- *Operations, Maintenance, and Administration costs will be reduced by 25% by 1996 and would be held through to 2002.*
- *Planned capital expenditures would be reduced by \$10 billion between 1993 and 2002.*
- *The debt/equity ratio will be improved to about 60/40.*
- *Ontario Hydro will reduce its work force by 6,000 at a cost of \$500 million.*
- *The Corporation will promote the emergence of a widening range of energy services, green technologies, and alternative technologies.*

- *The new Ontario Hydro will be more closely involved in joint undertakings with customers in the electricity supply business as well as in the energy services and demand side.*
- *Hydro intends to track market conditions and the plans of its customers much more closely in making its own future plans.*
- *Special rates will be introduced for surplus capacity to supply incremental industrial consumer needs.*

HOLDING THE LINE ON RATES

There will be no rate increase in 1994. We are still convinced that our measures to reduce our costs and debt will allow us to keep any increases to the rate of inflation or lower for the rest of the decade.

1993 RESTRUCTURING COSTS

– A ONE-TIME PROVISION

In December 1993, Ontario Hydro reclassified its three equity accounts into one retained earnings account. This reclassification allows the Corporation to write off one-time restructuring costs. It does not eliminate any obligations imposed by the Power Corporation Act nor does it have any impact on Hydro's level of debt or on its ability to repay debt.

The Board of Directors approved a total restructuring provision in the range of \$2.9 – \$3.5 billion against 1993 net income to be absorbed by retained earnings. This provision includes the previously estimated \$1.6 billion cost and additional amounts for the write-off of assets of uncertain or doubtful future value that were being carried on Hydro's balance sheet. Allowances have also been made for the possible write-off of generating capacity surplus to Hydro's future needs. It is important to note that these additional amounts for the write-offs of assets are non-cash transactions. The exact total of the restructuring provision will be confirmed at the February board meeting pending completion of a review of capital expenditures and capacity requirements.

For 1993, the Corporation will have little or no operating loss, which represents an improvement on the \$200 million loss that was forecast earlier. This is due in large part to improved generation performance and reduction of Operations, Maintenance, and Administration (OM&A) costs by 5% or \$100 million.

The total restructuring provision, once applied to the retained earnings account will result in a debt ratio of between .90 and .92, but will enable Hydro to maintain its rate commitments while enhancing future financial flexibility. Hydro is forecasting a net income of more than \$600 million in 1994.

**AGGRESSIVE SAVINGS IN OPERATIONS,
MAINTENANCE & ADMINISTRATION (OM&A)**

Approximately 75% of Ontario Hydro's costs are fixed. In the short term, it means that any available cost improvements must be made in the remaining 25% of our costs which are largely made up of Operations, Maintenance & Administration costs. However, in the long term, the Corporation is working to substantially reduce many of its fixed costs.

In 1994, OM&A costs are expected to be \$450 million below 1993 levels. This is \$700 million below those forecast last year.

Of the total OM&A costs, 65% are associated with labour costs. This remains one of the few areas where Hydro can control costs. A reasonable settlement with the Power Workers' Union will help Hydro meet its commit-

ment to no real rate increases for the rest of the decade.

CAPITAL COST CONTROL AHEAD OF SCHEDULE

Over the past two years, the Corporation has undertaken many initiatives to control costs. Capital programs have been reduced by \$24 billion. The Corporation's original target was \$10 billion reduction by 2002. Restructuring of the corporation's long-term debt will also reduce interest charges. The business units have identified an additional \$1 billion of potential capital expenditure reductions.

The capital investments which are proceeding are those associated with improving the environmental performance of the system and those necessary to sustain safety and service reliability. These include needed distribution and transmission stations and line reinforcements.

WORK IS UNDERWAY TO IMPROVE THE DEBT/EQUITY RATIO

The Corporation is working in all areas to control operating costs, improve cash flow, and cut back capital expenditures. By continuing this course, the debt/equity ratio will be improved.



OUR WORKFORCE SEPARATION PROGRAMS WILL PAY OFF IN 1.7 YEARS

Since the introduction of the voluntary separation programs in the fall of 1992 Ontario Hydro has reduced its regular workforce by 23.9% to 22,500 from 29,581.

As of December 1, 1993, these cutbacks included a 26.8% reduction in executive staff, 42.8% in supervisory staff, 24.2% in non-supervisory Management and Professional staff, and 19.9% in Power Workers' Union represented staff. In addition, there has been a reduction of 4,000 contract staff.

The total cost of the staff separation programs was \$624 million (including a pension liability of \$396 million). The

resulting annual labour savings is approximately \$404 million, giving a payback of 1.7 years.



Unfortunately, the staff adjustments during restructuring resulted in a decline in the representation of women in the total workforce to 19.8% from 22%. Despite this situation, the percentage of women in the executive levels increased to 10.9% from 8.2%.

Representation of visible minorities at the executive levels also increased. Hydro was able to maintain the relative percentages of visible minority and Aboriginal employees despite the restructuring.

SUSTAINABLE ENERGY DEVELOPMENT AND ONTARIO HYDRO

The Task Force Report on Sustainable Energy Development was presented in 1993. Since then, Hydro's business units have begun to identify the challenges associated with its implementation.

The report's recommendations also offer opportunities to apply the principles of Integrated Resource Planning to strengthen energy efficiency and demand management programs.

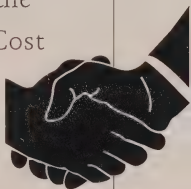
Hydro is pledged to integrating environmental and economic factors into the decision-making process. Part of this process will be to adopt Full Cost Accounting to help guide decision making. The Corporation will strengthen energy efficiency and demand management programs and shift from compliance to leadership on environmental performance.

Hydro is also determined to see that its efforts reach out beyond the Corporation. The Corporation will use its procurement power to promote the market for sustainable products, and its research activities to develop sustainable energy technologies. Plans are underway for the introduction of new working relationships with stakeholders, communities, and governments as well as an increased emphasis on international market opportunities for sustainable energy use.

To garner comment from both employees and major stakeholders, roundtables were launched in 1993 to discuss the Task Force Report on Sustainable Energy Development and how Hydro intends to implement the recommendations. Business representatives are particularly interested in the implications associated with Full Cost Accounting.

**ENERGY SERVICES AND ENVIRONMENT IS
WORKING CLOSELY WITH OUR CUSTOMERS**

The Energy Services and Environment (ES&E) business group is pursuing a strategy to provide a range of options to better meet customer needs. ES&E will promote energy efficiency by



providing consumer-driven, cost-effective energy efficiency initiatives, and pursuing low-cost and non-cash initiatives. Numerous innovative rate options, including flexible rates, are being considered.

To ensure customer retention, Hydro will create and implement rates that take advantage of Hydro's lower marginal costs. Customized energy management initiatives will also be offered. Ontario Hydro will work with government agencies and business partners to support economic development in accordance with public policy and the need of our customers and stakeholders. Plans have been made to provide training for industry staff, transferring Hydro expertise to the marketplace. The Corporation will look for opportunities for product endorsement and strategic procurement to stimulate and encourage the development and use of energy efficient technologies.

Each stage of implementation will include consultation with employees, major customers, key stakeholders, and various levels of government.

NEW OPPORTUNITIES FOR ONTARIO HYDRO INTERNATIONAL/ONTARIO HYDRO TECHNOLOGIES

Ontario Hydro International (OHI) is an incorporated, wholly-owned subsidiary of Ontario Hydro. It is forging a path for itself as a leader in energy efficiency and sustainable development in the rapidly changing global marketplace.

Much of OHI's potential business is in the developing world where economic development and environmental stewardship must be effectively integrated. Sustainable development is a key principle of OHI's operating mandate.

OHI has joined forces with Hydro-Quebec International and Power/Asia Assets Corporation, a subsidiary of Power Corporation of Canada, to invest in the explosive growth of Asia's energy sector through its consortium Asia Power Group/Groupe Energie Asie Inc. (APG). APG will target investments in power production projects that meet appropriate environmental standards, as well as transmission facilities and local utilities.

Ontario Hydro Technologies, a newly formed organization within Ontario Hydro Enterprises, has a mandate to commercialize proprietary technology and to

invest in non-proprietary sustainable development technology. Ontario Hydro Technologies has advanced its goal of identifying, developing, and marketing sustainable development technologies by joining the federal and provincial governments in forming the Ontario Centre for Environmental Technology Advancement. The centre will be a clearing house for industry ideas and information to small and medium-sized businesses.

To spur the development of marketable sustainable development technologies, OHT has been given a target of increasing revenues from Hydro-developed products to \$22 million annually.

AGREEMENTS MADE WITH FIRST NATIONS

Settlements of past grievances were signed with five of Ontario's First Nations in 1993. At the signing of the agreement with the Wabaseemoong Independent Nations of One Man Lake, White Dog and Swan Lake, Mr. Strong said, "We apologize...for our failure to respect your dignity and your rights." Chief Eric Fisher said that, "Despite years of bringing (the grievances) to Hydro's attention,

...Hydro (now) began to respect our culture, our respect for our ancestors and elders, and how land issues are so tied to the health and identity of our people.

These settlements demonstrated Hydro's continuing progress in strengthening relationships with First Nations and established Hydro as leader in this area. Additional settlements will be made in 1994.

GLOSSARY

OM&A PROGRAM COSTS

OM&A Program Costs are the costs associated with operating, maintaining, and administering Hydro's generation, transmission, and distribution facilities.

CAPITAL PROGRAM COSTS

Capital Program Costs are costs associated with the construction, procurement, and commissioning of capital facilities.

DEBT OUTSTANDING

Debt Outstanding includes bonds and notes payable, short-term notes payable, other long-term debt, accumulated provisions, bank indebtedness; less unamortized foreign exchange gains or losses and investments held for interest rate management purposes.

EQUITY

Equity represents the amounts invested in the electricity system which have been contributed by customers, in the form of net income, or by the Province of Ontario.

